No. 16,014

IN THE

United States Court of Appeals

For the Ninth Circuit

UNITED STATES OF AMERICA,
Appellant,

vs.

ASHBY O. STEWART, Executor of the Last Will and Testament of Mary W. Stewart, Deceased,
Appellee.

On Appeal from the Judgment of the United States District Court for the Northern District of California.

BRIEF FOR THE APPELLEE.

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OPINION BELOW.

The opinion of the District Court (Tr. 34-49) is reported at 158 F. Supp. 25.

JURISDICTION.

This appeal involves federal estate taxes. The taxes in dispute plus interest in the total amount of $222,-357.11 were paid on or about August 24, 1954 (Tr. 55).

Claim for refund was filed on or about March 10, 1955 (Tr. 15-19), and the Commissioner of Internal Revenue rejected the claim on March 21, 1956 (Tr. 8, 10, 21, 23). Within the time provided in Section 3772 of the Internal Revenue Code of 1939 and on July 3, 1956, the taxpayer brought an action in the District Court for recovery of the taxes paid (Tr. 3-19). Jurisdiction was conferred on the District Court by 28 U.S.C., Section 1346. The judgment was entered on March 17, 1958 (Tr. 56-57). Within sixty-days and on May 2, 1958, a notice of appeal was filed (Tr. 58). Jurisdiction is conferred on this Court by 28 U.S.C., Section 1291.

QUESTIONS PRESENTED.

I.

Whether the Court below erred in holding that upon Mrs. Stewart's death, her interests in life insurance policies, premiums on which were paid from community funds, covering her surviving husband's life, were at no time the subject of transfers of property taxable under the federal estate tax laws;

II.

Whether the Court below erred in holding that the rights of beneficiaries to receive annuities upon the death of Mrs. Stewart under certain contracts between her and insurance companies, assented to by her husband, and relating to the deposit and dispo-

sition of community funds, were includible in Mrs. Stewart's gross estate for federal estate tax purposes only to the extent of one-half the value of said rights rather than the full value.

STATUTES INVOLVED.

These appear in the Appendix, infra.

STATEMENT.

Three issues were presented to the Court below. One of these issues (First Cause of Action) was conceded by the Government. A second issue (Second Cause of Action), that concerning the inclusion in Mrs. Stewart's gross estate of all or just part of the proceeds of life insurance annuity policies payable to her and upon her death to others, was decided by the Court below partly in favor of the Government and partly in favor of the taxpayer. The third issue (Third Cause of Action), that concerning the inclusion in Mrs. Stewart's gross estate of one-half the cash surrender value of insurance policies on the life of her surviving husband, was decided by the Court below in favor of the taxpayer. The Government has appealed from the determinations of the Court below adverse to it, excepting of course as to the first issue, as to which it acknowledged error.

The case was tried entirely on the pleadings and a written stipulation of facts (Tr. 34).

Ashby O. (or A. O.) and Mary Stewart were married in 1906 and their marital relationship continued until Mary's death on February 21, 1951. At all times pertinent to this case they were residents of California (Tr. 25, 34-35).

At the time of death of Mary W. Stewart there existed twenty-six policies of insurance covering the life of decedent's husband, Ashby O. Stewart. No part of the value of these policies was reported in the Federal estate tax return for the estate of Mary W. Stewart. Upon audit of that return the Commissioner of Internal Revenue determined that one-half of the $751,178.85 cash value of these policies at the time of her death, or $375,589.42, should be included in the decedent's gross estate (Stip. para. 17, Tr. 29).

These life insurance policies were purchased by payment of premiums out of the community property funds of Mr. and Mrs. Stewart (Stip. para. 17, Tr. 29).

Plaintiff and his wife Mary W. Stewart had no transactions and no agreements with respect to these insurance policies other than those disclosed by said policies and documents attached to said policies (Stip. para. 18, Tr. 30).

The following tabulation is a quick reference to certain pertinent rights under the respective policies:

Policies Under Which Wife Was Named Primary Beneficiary, and Others Named as Contingent Beneficiaries		Designation of Beneficiary Consented to by Wife		Right to Change Beneficiary or Surrender Policy Retained by Husband	
Number of Policies	Name of Insurer	Yes	No	Yes	No
1	Pacific Mutual		x	x	
1	Aetna		x	x	
8	Equitable	x		x	
2	Travelers	x		x	
1	Massachusetts Mutual	x		x	
2	Mutual of New York*		x	x	
2	Equitable	x		x	
3	New York Life	x			x
1	John Hancock	x			x
2	Aetna		x	x	

*Could not take cash surrender value.

Policies Under Which Daughter or Grandchildren Were Named Primary Beneficiaries, and Wife Named as Contingent Beneficiary		Designation of Beneficiary Consented to by Wife		Right to Change Beneficiary or Surrender Policy Retained by Husband	
Number of Policies	Name of Insurer	Yes	No	Yes	No
2	Mutual Benefit		x	x	
1	West Coast		x	x	

The Government contended that Mrs. Stewart's community property interest was includible in her gross estate under Sections 811(a), (c) or (d) of the Internal Revenue Code of 1939 (Tr. 45).

The Court below concluded that Mrs. Stewart's community property interest in these policies was in effect a right of protection; a right to upset during her lifetime as to one-half in the event that the proceeds were paid to a stranger on Mr. Stewart's death without her consent (Tr. 48-49). The Court concluded this right was extinguished upon her death (Tr. 49), and that with respect to this right there was no tax-

able transfer occasioned by the wife's death and there was no interest to which the estate tax would attach (Tr. 46, 47, 49), and therefore the Government was in error in including a value for these policies in the wife's taxable estate (Tr. 49).

In Schedule D of the Federal Estate Tax Return filed by the estate of the decedent, Mary W. Stewart (Exhibit "A" attached to Stip.), plaintiff reported certain annuity insurance policies, the proceeds of which were payable to named beneficiaries other than decedent or her estate, upon the death of the decedent. These policies were purchased through payment of premiums out of community property funds of plaintiff and decedent, and Mrs. Stewart was the insured. The total valuation of said proceeds upon the date of decedent's death was $130,416.16. Plaintiff reported only one-half of the full value of the said proceeds for estate tax purposes, or $65,208.08 (Stip. para. 15, Tr. 29).

In the audit of the aforementioned estate tax return the Commissioner of Internal Revenue determined that the above-mentioned life insurance reported in Schedule D of the estate tax return was the separate property of the decedent Mary W. Stewart, and increased the valuation thereof in the decedent's gross estate by an additional amount of $65,208.08, to a total valuation of $130,416.16, which was the full value of the said life insurance proceeds upon the date of the decedent's death (Stip. para. 16, Tr. 29).

Plaintiff and his wife Mary W. Stewart had no transactions and no agreements with respect to these

insurance policies other than those disclosed by said policies and documents attached to said policies (Stip. para. 18, Tr. 30).

In all these policies Mr. Stewart was described as the husband of the beneficiary. He was originally named a beneficiary and when his designation of beneficiary was changed he expressed his consent to or authorization of his wife's actions in the following manner:

In the John Hancock policies (Ex. D) this authorization in 1946 and 1948 is expressed, "The insured's husband, Ashby O. Stewart, hereby joins in the foregoing election of settlement option and authorizes and requests the company to comply with the terms hereof."

In the Aetna policies (Ex. E) this authorization in 1950 is expressed in a statement signed "Mary Woods Stewart, Annuitant" and "Ashby O. Stewart, husband of Annuitant", "Application is hereby made for payment of the cash value of Policy No. ..... issued on the life of Mary Woods Stewart. . . . The Company is hereby authorized to make any necessary change in beneficiary of said policy to enable the undersigned alone to surrender said policy as herein requested. Settlement of proceeds to be made in accordance with my letter of November 9, 1950". The letter of November 9, 1950 is written on the letterhead of A. O. Stewart, and is signed by Mary W. Stewart, and instructs as to the payment of the annuities.

In the Equitable policies (Ex. F) this authorization in 1948 is expressed, "I hereby agree to the fore-

going beneficiary provisions. Signature of Annuitant's husband".

In contrast the endorsement on the Fidelity policies (Ex. C) was a specific transfer of community rights as follows: "I, Ashby Oliver Stewart, am the spouse of the owner of policies Nos. 581822-581823 issued by your Company on the life of Mary Woods Stewart. I hereby relinquish any and all community property rights I may have in said policies and in all payments made or to be made thereunder by your Company, and in all premiums paid or to be paid in connection with said policies as the separate property of my said wife. . . ." Signed "Mary Woods Stewart" and "O.K., Ashby Oliver Stewart".

Both taxpayer and Government referred to Section 811(g) of the Internal Revenue Code of 1939, in support of their positions, the taxpayer contending further that under that section perhaps no part of the value of these policies was includible in the wife's estate.

The Court concluded that because these policies were annuity policies rather than insurance policies, Section 811(g) was not applicable (Tr. 41, 43). The Court further concluded that the wife's interest in the value of the proceeds which were payable upon her death was includible in her gross estate under Section 811(a) of the Internal Revenue Code of 1939, and also that her interest so includible was merely her community property interest which was one-half the value of such proceeds (Tr. 43, 44), excepting as to the Fidelity policies as to which the Court agreed

with the Government that since the husband had specifically transferred his community interest to his wife, the entire value of the proceeds payable under that policy was includible in the wife's gross estate.

ARGUMENT.

I.

THE COMMUNITY PROPERTY INTEREST OF THE WIFE IN THE INSURANCE POLICY COVERING HER HUSBAND'S DEATH, PREMIUMS FOR WHICH WERE PAID OUT OF COMMUNITY FUNDS, WAS A RIGHT OF PROTECTION WHICH WAS PERSONAL TO HER AND WAS EXTINGUISHED BY HER DEATH. SHE HAD NO PROPERTY INTEREST IN SAID POLICIES WHICH WAS AT ANY TIME THE SUBJECT OF TRANSFERS TAXABLE UNDER THE FEDERAL ESTATE TAX LAWS.

The Government contends that one-half the cash surrender value of insurance policies insuring the life of the surviving husband is includible in the gross estate of the deceased wife, where the premiums paid on those policies were paid out of community funds. The Government contends that the one-half of the cash surrender values of these policies on the date of the wife's death represented her "interest therein . . . at the time of her death" within the meaning of Section 811(a) of the Internal Revenue Code of 1939 requiring that there be included in the decedent's gross estate for Federal Estate Tax purposes the value at time of death of property "to the extent of the interest therein of the decedent at the time of his death".

It is conceded by the Appellee herein that the insurance policies were a form of community property

and the Court below so held (Tr. 45). It is also conceded that the wife has power to dispose by will of whatever disposable interest in community property she may have at the time of her death. The question at issue here is: What was the nature and extent of the community property interest of the decedent in the insurance policy at the time of her death, and was it something includible in her gross estate?

The Government's contention is predicated upon the Government's conclusion that "had the decedent herein so desired, it would have been completely proper for her to have made testamentary disposition of her share of these twenty-six insurance policies, and under the Probate Code of the State of California this disposition would have been effective" (Appellant's brief p. 20, repeated in effect p. 23, p. 19, p. 13). This is not the law. If it were so the Government would be correct in its contention. Both Judge Yankwich, the trial Judge in the case of *Waechter v. U. S.,* 98 F. Supp. 960 (W.D.Wash.), and Judge Hamlin in this case stated the law on this point to be to the contrary. Judge Hamlin concluded (Tr. 48) after referring to California Civil Code Section 172:

> "In the realm of insurance law, this last cited code section has been held to give the wife the right to upset the payment of one-half of the proceeds of policies on the husband's life to a stranger. *Mazman v. Brown* (1936), 12 C.A. 2d 272, 55 P. 2d 539. However, the wife's right to contest is not activated until the death of the insured husband, when the gift was completed.

Further, if she did not take any steps to invalidate the gift during her lifetime, it became valid upon her death. *Mayr v. Arana* (1955), 133 C.A. 471, 284 P. 2d 21.

"This interest which Mrs. Stewart had in the insurance policies was, in effect, a right of protection; a right to upset during her lifetime as to one-half in the event that the proceeds were paid to a stranger on Mr. Stewart's death without her consent. But this right of protection did not enure to the benefit of anyone on her death since her death extinguished this right. Both before and after her death he had the right to take the cash surrender value of these policies without her consent, because he had the management and control of the community property. It was only the dissipation of the cash surrender value during her lifetime by way of gift which she could prevent.

"However this right might be classified, I do not believe it comes within the purview of those subsections of the Internal Revenue Code cited by the Government. The principle of the *Waechter* case, supra, appears to me to be equally applicable to California community property law."

The *Waechter* case was affirmed by this Circuit, *United States v. Waechter,* 1952, 195 F. (2d) 963. (Appellant states in its brief p. 21 "affirmed on other grounds". This Appellate Court refused to hear issues not raised in the trial court, but the Court did affirm the judgment of the trial court.) The significance of the *Waechter* case as decisive of the exact issue involved in this proceeding cannot be more

clearly illustrated than by this Court's description of the case and of the trial court's conclusion therein as to the law. This Court said:

> "The theory on which the government defended below appears to have been simply that the cash surrender value of the policies was community property, hence the wife's interest was subject to her power of testamentary disposition under Remington's Revised Statutes of Washington, Sec. 1342. The trial court was of the opinion that no part of the cash surrender value was includable in view of the holding in *In re Knight's Estate,* 31 Wash.2d 813, 199 P.2d 89, decided in 1949. The Washington court there decided that in the case of policies payable on the death of an insured, nothing whatever becomes payable on the death of a beneficiary prior to the insured's death, and thus no interest in the policies or in the cash surrender value thereof passes to the heirs of the deceased beneficiary." 195 F.(2d) at 963-4.

This Appellate Court then goes on to say that "On its appeal the Government does not contend that the law of the state is otherwise than has been declared in the *Knight's Estate* decision. However, it seeks a reversal on a theory apparently not urged below. Its reliance here is placed on Section 811(e)(2) of the Internal Revenue Code . . ." The Court then refused to consider this theory and affirmed the judgment of the Court below.

The Section 811(e)(2) involved in the *Waechter* case and the part thereof which the Government urged in the appeal was repealed and was not in

effect at the time of Mrs. Stewart's death (Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 402 (26 U.S.C. 1952 ed., Sec. 811); Revenue Act of 1948, c. 168, 62 Stat. 110, Sec. 351). However, the basis for taxability under that section as considered by the trial court is the same as the basis for taxability under Section 811(a) invoked by the Government in this case. So the only difference between the *Waechter* appeal and the appeal in this case is that the Government is now contesting the same conclusion of law which it accepted in the *Waechter* appeal as to the deceased's wife's interest upon her death in a policy of insurance covering her surviving husband's life.

There has intervened between the time of the *Waechter* appeal and the present time the decision of the U. S. District Court (S.D. California Central Div.) in *California Trust Company v. Riddell,* 136 F. Supp. 7. In that case the Court without any reference whatever to the *Waechter* case merely concluded that since the wife had a community interest in a policy on her husband's life the Government was correct in including one-half the cash surrender value of that policy in her gross estate. Judge Hamlin, in this proceeding, after referring to the *California Trust Co.* case, then referred to the *Waechter* case and stated, "I am more persuaded by the reasoning of the trial court in this case (*Waechter*) and by the fact that that decision was upheld by the Court of Appeals."

In the case of *Mayr v. Arana* (1955), 133 C.A. (2d) 471, 284 P. (2d) 21 (District Court of Appeals, Sec-

ond District, Division 2, Calif.), under a policy insuring the husband's life the proceeds payable on his death were to be paid first to his wife as primary beneficiary, with any unpaid balance to be paid upon her death to his mother as secondary beneficiary. The husband died and a few hours after his death the wife died. The husband's mother claimed the proceeds as secondary beneficiary. The wife's parents claimed the proceeds as her heirs. The Court decided that under the policy the balance of the proceeds were payable upon death of the wife to the secondary beneficiary, and the Court then considered the question, "In view of the fact that the premiums on the insurance policy were paid with community funds, did the estate of decedent's wife have a community interest in the proceeds of the insurance policy". The Court's decision on this question was as follows:

> "This question must be answered in the negative for two reasons:
>
> (1) While it is true that under the California decisions the husband cannot make a gift of community property without his wife's consent, it is likewise settled that unless the wife desires to void the gift and takes action to set it aside the gift is valid. (*Blethen v. Pacific Mut. Life Ins. Co.,* 198 Cal. 91, 101 (7), 243 P. 431; *Pomper v. Behnke,* 97 Cal.App. 628, 638 (12, 13), 276 P. 122.)
>
> In the instant case the foregoing rule is applicable since the wife, knowing the terms of the policy, never at any time took any steps to assert her community rights thereunder. On the contrary, the record discloses that the agent who

sold the policy testified that Mrs. Ramona Arana stated at the time the policy was issued that she felt the proceeds, if she were not living, should go to the decedent's mother. Since the wife took no steps to invalidate the gift, assuming it to be such, prior to her death, it became valid upon her death. (*Italian American Bank v. Canepa,* 52 Cal.App. 619, 621 (1), 199 P.55.)

(2) There was not a gift of the proceeds of the policy to respondent since the decedent could have given one half of the proceeds to his mother without his wife's consent, but in consideration of the wife's consenting to the policy whereby she became the primary beneficiary of the entire amount named in the policy she released her community interest, in the event of her death prior to her mother-in-law's, to respondent. (Cf. *Trimble v. Trimble,* 219 Cal. 340, 343 (4), 26 P.2d 477.)'' 133 C.A. (2d) at 477-478.

In its brief the Appellant has consistently confused the right of a surviving wife in the *proceeds* of life insurance on her deceased husband's life, with the right of a wife at time of her death in insurance policies covering the life of her living husband. These are separate and distinct rights covering separate and distinct property. The particular issue under discussion here does not involve *proceeds* of the policies on the husband's life—he is still living; it involves only the right of the wife at the time of her death in an insurance *policy contract* insuring the life of her surviving husband.

Appellee concedes that if the husband had died first and the policy proceeds had been paid to Mrs. Stew-

art, she would have received them as her separate property, one-half traceable to her own share of community property and one-half traceable to her husband's share of community property. This result follows because at her husband's death the proceeds, as property, came into existence, and a previously existing contingent or inchoate gift became complete and vested. (*In re Miller Estate* (1937) 23 Cal. App. (2d) 16, 71 P. (2d) 1117.) In this case, however, the issue does not involve proceeds of a policy but involves the wife's community property interest at time of her death in the policy or contract which provides for a contingent inchoate gift whether the gift be to her or to a third person, or both.[1]

The only rights which the wife possessed in these contracts at the time of her death were (A) where she is named beneficiary, a right contingent upon her surviving her husband to acquire the proceeds (*Mayr v. Arana, supra*), and, (B) where a third party is named beneficiary, a right to object to the vesting of one-half of the completed gift *after* the death of her husband (*Blethen v. Pacific Mutual Life Ins. Co.,* 198 Cal. 91, 243 P. 431). She alone had that right of objection which she could exercise or not as she might elect, and if she failed to exercise that right the com-

[1]Where the insured has not reserved the right to change beneficiaries, the named beneficiary has a vested right to obtain the proceeds upon the death of the insured, *contingent* upon surviving the insured; where the insured has reserved the right to change beneficiaries, the named beneficiary's interest prior to the death of the insured is that of a mere expectancy of an incompleted gift (*In re Castagnola's Estate,* 68 C.A. 732, 736, 230 P. 188 (1924)).

pleted gift to the third party beneficiary was valid immediately upon its vesting at time of husband's death. This right of protection, or this right to object, was personal and could not be exercised by her representatives or heirs after her death.[2] Upon her death this right merely ceased to exist—it was not transferred, nor did her death generate the transfer of any property. She had a right if she lived to cause a transfer of property to be made either by exercise or non-exercise of this right to object, but upon her death before the property represented by the proceeds came into existence, her right to exercise some future dominion over that property merely ceased or terminated. There was nothing identifiable over which she had the power of control under the policy at time of her death which was transferred upon her death. As the Court below concluded, her "right of protection did not enure to the benefit of anyone on her death since her death extinguished this right" (Tr. 49).

These community property rights of the wife in an insurance policy covering the life of her husband is something akin to a life estate in property terminating upon her death, or to a right as a joint tenant. Upon her death her right as owner of the half, or contingent owner of the whole became extinguished.

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[2]Even the right to object to an outright gift of community property is personal to the wife.

> "The right to avoid . . . is personal to the wife . . . it seems that if the wife dies during the lifetime of the husband without having taken steps to disaffirm the transaction, it becomes valid in its entirety." 10 Cal. Jur. 2d, Community Property, Section 80.

As the right of a deceased joint tenant in joint tenancy property was not includible in his gross estate until special legislation was enacted to specifically include it, just so these community property rights of the wife contingent upon her surviving her husband, and extinguished upon her predeceasing her husband, cannot be included in her gross estate upon her death. This conclusion applies whether the wife be named beneficiary with or without her consent, or whether a third party be named beneficiary with or without her consent.

It is true that in cases of divorce or in cases involving wrongful death caused by a spouse beneficiary, the cash surrender value of a policy is recognized as a measure of community property in determining property rights of the husband and wife at a given time. But at no time did the wife have the right to compel the husband to cancel the insurance policy or demand or secure the cash surrender value of the policy.[3] Under Section 172 of the California Civil Code the husband is made the manager of the community personalty. He had the exclusive right to use it as he saw fit excepting only that he could not make a gift of it without the consent of his wife. As the Court below pointed out (Tr. 49), "both before and after her death he (husband) had the right to take the cash surrender value of these policies without her

[3]The "cash surrender value" means the cash value, ascertainable by established rules, of a contract of insurance which has been abandoned and given up for cancellation to the insurer by the person having the contract right so to do. *In re Knight's Estate, supra.* Husband could not be compelled to cancel the contract. *Waechter—Dist. Ct.*, 98 F. Supp. at 962.

consent, because he had the management and control of the community property. It was only the dissipation of the cash surrender value during her lifetime by way of gift which she could prevent." Upon her death, therefore, she had no interest in the cash surrender value which was transferred or transferable.[4] The insurance contract was not changed by her death and rights under this contract are determined by the law of contracts and not the law of succession (*Turner v. Metropolitan Life Ins. Co.,* 56 Cal. App. (2d) 862, 133 P. (2d) 859; beneficiaries take by contract and not by succession; *In re Estate of Ward,* 127 Cal. App. 347, 15 P. (2d) 901). Once the contract was entered into, her community property rights in the money used to pay the premiums changed from an absolute right to that money to those rights in the insurance contract herein described and those rights were rights which expired upon her death where she predeceased her insured husband. She had no right to dispose of the cash surrender value by will or otherwise and the California laws make no provision for collection by her personal representatives of any part of this cash surrender value.

On page 24 of its brief the Government argues that, "Because of her death, she ceased to hold an interest

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[4]The estate tax is a tax on the *transfer* of the net estate (Section 810, Internal Revenue Code of 1939), and the net estate includes the value at time of death of all property to the extent of the decedent's interest therein, and the value of certain other property as particularly specified in the Code (Section 811). Unless there is an actual transfer upon death or a transfer specifically described by the Statute, there can be no federal estate tax.

in the policies, and such interest passed to her estate, to her husband, or to the beneficiaries of the policies". There was no more a "passing" of property in this situation than in the situation of a deceased life tenant or a deceased joint tenant. The interest of the survivors existed by virtue of the original acquisition which created the life tenancy or the joint tenancy and not by virtue of any passing of property from the deceased life tenant or joint tenant. In this case, upon the death of the wife her interest merely expired and the interest of the survivors existed by virtue of the terms of the insurance contract and not by virtue of any passing of property from the deceased.

On page 25 of its brief the Government argues that if the husband, by naming a beneficiary, made a gift, the wife could avoid it, and when she did not avoid it her failure to do so caused a transfer of property upon her death. The fallacy of this argument is, first, that her right to avoid the gift, assuming there was a gift, was contingent upon her surviving her husband; and second, as to 17 of the 26 policies she was the primary beneficiary. Thus, there either was no gift by the husband of her property or, under the rule of law stated in the *Mayr v. Arana* case, *supra,* she gave up her community interest for an adequate consideration which was a right to receive *all* the proceeds contingent upon her surviving her husband.

As to 17 of the 26 policies, Mrs. Stewart expressed her assent in one way or another to the designation of herself as primary beneficiary and others as con-

tingent beneficiaries. In the *Ettlinger v. Connecticut General Life Insurance Company* case, 175 Fed. (2d) 870, a wife claimed an interest in proceeds of an insurance policy on her husband's life under which his children were designated as beneficiary, to which designation she had given her assent in writing. This Court, in denying the wife's claim, held that "an unqualified assent that the proceeds of the policies be paid to the designated beneficiary is a sufficient consent in writing that the wife gives up her community interest in the policy". This decision means nothing more than that the wife by her assent has given up her right to object after the death of her husband to the payment of the proceeds of the policy to a third party beneficiary.

No matter how this problem is analyzed we come back to the fundamental premise that the wife's community property interest in the insurance contract is merely the right to object to a payment of the proceeds to a third party beneficiary which right is contingent upon her surviving her husband; or it is a right to secure the proceeds of the policy where she is named beneficiary, but again contingent upon her surviving her husband and contingent also upon her designation as beneficiary not being revoked. Where she dies before her husband these community property rights of protection die with her. The rights of all other persons have been and are established under the contract and there is no passing or transfer of any property interest in the policies resulting from, or effective upon her death, and therefore no transfer

which would be subject to the taxing provisions of the Federal Estate Tax laws.

It is respectfully submitted that the decision and judgment of the District Court with respect to this issue is correct and should be affirmed.

II.

THE ANNUITY CONTRACTS OF THE WIFE, TO WHICH HER HUSBAND EXPRESSED HIS ASSENT, INVOLVED THE DEPOSIT AND DISPOSITION OF COMMUNITY PROPERTY WHICH REMAINED COMMUNITY PROPERTY UNTIL THE DEATH OF THE WIFE, EXCEPTING AS TO THE FIDELITY POLICIES WITH RESPECT TO WHICH THE HUSBAND SPECIFICALLY TRANSFERRED HIS COMMUNITY INTEREST TO HIS WIFE, SO THE ONLY AMOUNTS INCLUDIBLE IN HER GROSS ESTATE WITH RESPECT TO THESE POLICIES IS ONE-HALF THE VALUE OF THE PROCEEDS PAYABLE UNDER ALL POLICIES EXCEPT THE FIDELITY POLICIES, AND THE ENTIRE VALUE OF THE PROCEEDS PAYABLE UNDER THE FIDELITY POLICIES.

The Government contends that the value of annuities payable after her death to beneficiaries named under seven annuity policies which were issued to the decedent in 1934 or 1935, should be included in full in the estate of the decedent, notwithstanding premiums which were paid for these policies were paid out of community funds. The Government contends that the decedent's interest in the annuities was acquired by her as her separate property because she had acquired her right thereunder by an instrument in writing, and under Section 164 of the Civil Code of California there is a presumption that any prop-

erty acquired by a married woman by an instrument in writing is her separate property. The Government also contends that, "Although it is felt that under the California law these policies have been the separate property of decedent ever since they were first issued to her, should the Court for some reason reach a contrary decision . . . the policies became separate property of the decedent at the time her husband signed the change of beneficiary forms", and in support of this contention the Government cites the case of *Ettlinger v. Connecticut General Life Insurance Company,* 175 Fed. (2d) 870.

The taxpayer contends that the annuities and the right to annuities were community property and therefore only one-half of the value of the beneficiary's right to receive the annuities after the wife's death is includible in her gross estate for federal estate tax purposes, excepting as to the annuities under the Fidelity policies which are conceded to be her separate property.

The Court below concluded:

> "It was stipulated that the policies were procured after the marriage and premiums were paid with community funds. Under California law the policies were, prima facie, community property. *Grimm v. Grimm* (1945), 26 C.2d 173, 157 P.2d 841. . . .
>
> "There are a number of ways by which these policies could become the separate property of Mrs. Stewart, but the only plausible explanation according to the facts as they existed is that they became such, if at all, by gift from Mr. Stewart

to Mrs. Stewart. Indeed, that is what the Government contends occurred.

"However, there is no substantial evidence in the record before me that there was such a gift, except as to the Fidelity policies; in fact, all the evidence is to the contrary. When Mrs. Stewart requested the insurance companies to change beneficiaries or mode of settlement, Mr. Stewart concurred in writing a majority of the time. His consent to these changes would not be necessary if the policies were Mrs. Stewart's separate property. As stated above, in 1950 Mr. Stewart signed a document whereby he very definitely relinquished his community property rights in the Fidelity policies. As to those policies there is no doubt that they were Mrs. Stewart's separate property at the time of her death, but the fact that he saw fit not to do the same thing with his interest in the other policies is strong evidence that he did not intend to make a gift of them, but rather intended to retain his community interest." (Tr. p. 40-41.)

The Court thereafter pointed out that just before her death Mrs. Stewart arranged for monthly payments to herself of a certain amount for a definite period while she lived, and to her daughter in the event of her death prior to the expiration of the designated period, and the Court concluded:

"This right to receive the monthly payments was an interest in property which the decedent owned at the time of her death and is includible in her estate under Sec. 811(a). However, the monthly payments she did receive prior to her death, and, therefore, the right to receive those

payments, was a community asset. Mrs. Stewart's interest in the payment and the right to payment was only one-half thereof because of the operation of the community property laws. Therefore, one-half of the proceeds would be included in her estate.

"The proceeds of the Fidelity policies would be an exception to this rule. As was mentioned earlier, Mr. Stewart relinquished his community property rights in those policies prior to Mrs. Stewart's death and they thus became her separate property. As her separate property all the proceeds would be included in her gross estate." (Tr. p. 43-44.)

The Government argues that the presumption that property acquired by the wife in her own name is separate property is "evidence", that although the presumption is rebuttable there was no evidence to rebut it, and therefore the conclusion of the Court was contrary to the evidence (Appellant's Brief, p. 29). The presumption that property acquired during marriage is community property is also "evidence", and the presumption that property acquired with community funds continues to be community property is also "evidence", and the stipulation that the premiums paid for the annuities were paid out of community funds is also "evidence", and the inference of community property arising from the requirement of the insurance companies that Mr. Stewart express his assent is also "evidence", and further the fact that the husband executed a specific assignment of his rights in the Fidelity contracts to his wife as her

separate property and did not do so with respect to the other contracts is also "evidence". The Court below considered all of this evidence, and its finding that the evidence establishes that there was no gift from the husband to the wife, excepting as to the Fidelity policies, is binding upon appeal. (Rule 52(a), Federal Rules of Civil Procedure; *Rollingwood Corp. v. Commissioner* (1951-CA-9), 190 F. (2d) 263—notwithstanding facts were stipulated.)

Prudential Insurance Company v. Harrison, 106 Fed. Supp. 419 ((1952) SD-Central Division, California), involved a situation where a husband convicted of manslaughter for killing his wife made a claim as a beneficiary named in an insurance policy issued to his wife on her life, the premiums for which policy had been paid with community property. The Court after discussing separate property and community property held that the policy and the proceeds thereof were community property and not separate property of the wife, and therefore half the proceeds belonged to the husband as his part of the community. The Court concluded also that the husband could not collect the other part of the proceeds because of the statute preventing him from gaining from his own wrongdoing. In holding that the policies and the proceeds were community property the Court emphasized, "Community property is the rule, separate property the exception thereto", and the Court thereupon cited DeFuniak's "Principles of Community Property 1943", stating, "It is usually considered by most courts that, when a spouse dur-

ing marriage, takes out a policy on his or her own life and the premiums are paid from community funds, the policy represents community property".

In the case of *Union Mutual Life Insurance Company v. Broderick,* 196 Cal. 497, 238 Pac. 1034 (1925), a husband named his sister in place of his wife as a beneficiary under an insurance policy purchased with community funds in consideration for his sister making him two loans of $1,000, and other consideration, and the question arose as to whether the husband had made a gift of the policy to his wife prior to the naming of his sister as beneficiary. The trial court found that there was no gift and the Appellate Court held that the finding that the husband did not make a gift of the policy to the wife was controlling on appeal.

Acceptance by this Court of the lower Court's findings would alone require affirmance of the decision of the Court below. But Appellant's interpretation of Section 164 of the Civil Code of California seems to be so far at variance with the true meaning and effect of that Section that some comment thereon is required.

Section 164 of the Civil Code provides first:

> "All other property acquired after marriage by either husband or wife, or both, including real property situated in this State . . . is community property."

In this case Mr. and Mrs. Stewart gave a sum of money to an insurance company who contracted with Mrs. Stewart to pay annuities to her, or to her named

beneficiaries, the first of whom was her husband. It is stipulated that the money paid to the insurance company was community property (Stip. para. 15, Tr. 28). The presumption arises immediately that the annuities and the right to annuities attributable to the investment of the community funds in the annuity contract is community property.

Section 164 continues:

> "but whenever any real estate or personal property or any interest therein or encumbrance thereon, is acquired by a married woman by an instrument in writing, the presumption is that the same is her separate property . . ."

In this case Mr. and Mrs. Stewart delivered community funds to the insurance company who contracted with Mrs. Stewart to in effect return it in the form of annuities at her direction. Is this "personal property . . . acquired by a married woman by an instrument in writing" within the meaning of Section 164? The presumption of separate property established by Section 164 does not apply to instruments which do not actually convey a *title in property.* (*Pacific Tel. & Tel. Co. v. Wellman,* 98 C.A. (2d) 151, 219 P. (2d) 506 (1950); *Estate of Inman,* 148 A.C.A. 975, 307 P. (2d) 953 (1957).) The contract between Mrs. Stewart and the insurance company was merely an arrangement for *disposition* of community property deposited with the company by Mr. and Mrs. Stewart. Mrs. Stewart might have directed the company to return the money to her and in that event the money would still be community

property. It is difficult to see how this contract can be construed as conveying title to property to Mrs. Stewart.

Section 164 continues:

> ". . . except; that when any of such property is acquired by husband and wife by an instrument in which they are described as husband and wife, unless a different intention is expressed in the instrument, the presumption is that such property is the community property of said husband and wife."

All of the contracts with the insurance company specifically describe Mr. and Mrs. Stewart as husband and wife. There is nothing in the contracts indicating any intention that something was to be acquired as the separate property of Mrs. Stewart; to the contrary, the contract indicates a joint endeavor to *dispose* of community property in a specific way. It is also significant that Mr. Stewart was required to express his assent or authorization to change of beneficiaries in all of the policies, indicating quite clearly that the insurance companies did not look upon Mrs. Stewart's rights as her separate property. If they had thought her interests were her separate property they could have relied upon the final sentence in Section 164 which provides:

> "The presumptions in this section mentioned are conclusive in favor of any person dealing in good faith and for a valuable consideration with such married woman or her legal representatives or successors in interest, and regardless of any change in her marital status after acquisition of said property."

The insurance companies must have recognized the community property character of the money paid to them as premiums for the contracts. It is stipulated herein that the money so used was community property, and that Mr. Stewart, as Executor of Mrs. Stewart's estate, reported the value of the annuities in the federal estate tax returns as community property (Stip. para. 15, Tr. 28). The Court below was correct in concluding that the value of the annuities was community property and that there is nothing in the evidence to justify a contrary conclusion.

The foregoing argument establishing that the annuity contracts represented nothing more than a contract for a deposit and disposition of community property, the interest therein at all times continuing to be community property, refutes not only the Government's contention that the right to annuities was the separate property of the wife under Section 164 of the California Civil Code, but also the Government's alternative contention that the husband's assent to the execution of the policy constituted a gift to his wife of the community property deposited with the insurance company. However, since the Government refers to the *Ettlinger* case, supra, in support of this alternative contention, a discussion of this case would seem necessary.

The *Ettlinger* case involved a claim by a wife of part of the proceeds under an insurance policy covering the life of her deceased husband, which proceeds were payable to children who were named by the husband as beneficiaries under the policy, and whose

designation of beneficiary was assented to by the wife. The Court held that there was no other reason for the expression of consent by the wife except to record her agreement relinquishing her community property interest in the policy. The case is not applicable to the issue here involved. The case involves the right of a wife in proceeds under life insurance policies, and not the right of a husband in annuity contracts, premiums for which were paid out of community funds; and the case involves the effect of a consent by the wife to the payment of proceeds to a beneficiary designated by the husband; and not the effect of a consent by the husband to his wife's contract. The *Ettlinger* case involved a contract made by the husband which was valid without the consent of his wife; whereas here there is involved a contract made by the wife which would have been invalid and void without the consent of the husband.

As has hereinbefore been pointed out, it is stipulated in this case that the deposit of money with the insurance companies as premiums for the annuity policies, was a deposit of community funds. The insurance companies required an expression of assent by Mr. Stewart as shown by the policies or policy endorsements (See supra, p. 23). This expression of assent, excepting as to the Fidelity policies, was not in any sense a transfer of property but was nothing more than an authorization by Mr. Stewart that Mrs. Stewart, as his agent or as agent for the community, could contract with respect to the community property. Without this authorization the contract would

have been invalid and void because under Section 172 of the California Civil Code the husband has exclusive management and control of the community property. Under this section the wife has no power to dispose of the community property, or to enter into contracts for the sale and exchange thereof. *La Rosa v. Glaze,* 18 C.A. (2d) 354, 63 P. (2d) 1181 (1936); *Newell v. Brawner,* 140 C.A. (2d) 523, 295 P. (2d) 460 (1956). In the *La Rosa* case, the Court states:

> "The evidence is undisputed that . . . the subject of this litigation was the community property of Mr. and Mrs. Glaze. The husband, therefore, had the management and control of the property (Secs. 161a and 172 Civ. Code; 13 Cal. Jur. 819, Sec. 25). The evidence is also uncontradicted that the wife was not authorized by her husband, either as his *agent* or otherwise, to sign the contract . . . Nor is there any evidence that he thereafter ratified the contract. *The purported contract was therefore unauthorized and void.*" (Emphasis added.) 18 C.A. (2d) at 357.

In the *Newell* case, the Court states:

> "The bill of sale executed by the wife was ineffective to convey title to the community property, or any part of it, to defendant. (Civ. Code para. 172.) 140 C.A. (2d) at 526."

The validity of these insurance policies contracted for by the wife as the insured for the deposit of a premium paid from community funds, must depend upon an appointment by or an authorization from her husband to act as his agent. Whatever rights were accorded the wife under these contracts must neces-

sarily have been rights exercisable by her only as agent for her husband or the community. In the *Ettlinger* case the Court pointed out that there was no reason for the wife to consent to a contract covering community personal property except to relinquish an interest therein; whereas in this case the husband's assent was essential as a delegation of authority to his wife to act as his agent to preserve the validity of the contract. Had the subject of the contract been the separate property of the wife his assent would not have been necessary.

The record in this case clearly supports the conclusion of the Court below that the subject matter of the annuity contracts involved community property and continued to be community property up to the time of death of the wife, excepting as to the Fidelity policies as to which the husband specifically transferred his community interest to his wife. The decision of the lower Court should be sustained.

CONCLUSION.

It is respectfully submitted that the Court below was correct in concluding (1) that but one-half the value of proceeds payable under annuity policies after the death of Mrs. Stewart are includible in her gross estate for federal estate tax purposes, excepting that as to the Fidelity policies the entire value of such proceeds are includible, and, (2) that no part of the cash surrender value or any other value of the insurance policies covering the life of her surviving

husband is includible in her gross estate, and the decision of the Court below should be affirmed.

Dated, San Francisco, California,
August 28, 1958.

Respectfully submitted,
GEORGE H. KOSTER,
Attorney for the Appellee.

Of Counsel:
RICHARD W. GRAHAM.

(Appendix Follows.)

Appendix.

Appendix

Civil Code of California:

Sec. 161a. *Community property; interests of parties defined.*

The respective interests of the husband and wife in community property during continuance of the marriage relation are present, existing and equal interests under the management and control of the husband as is provided in sections 172 and 172a of the Civil Code. This section shall be construed as defining the respective interests and rights of husband and wife in community property (Added Stats. 1927, c. 265, p. 484, Sec. 1.)

Sec. 162. *Separate property; wife.*

SEPARATE PROPERTY OF THE WIFE. All property of the wife, owned by her before marriage, and that acquired afterwards by gift, bequest, devise, or descent, with the rents, issues, and profits thereof, is her separate property. The wife may, without the consent of her husband, convey her separate property. (Enacted 1872)

Sec. 164. *Community property; presumptions as to property acquired by wife; limitation of actions.*

All other property acquired after marriage by either husband or wife, or both, including real property situated in this State and personal property wherever situated, heretofore or hereafter acquired while domiciled elsewhere, which would not have been the separate property of either if acquired while domiciled in

this State, is community property; but whenever any real or personal property, or any interest therein or encumbrance thereon, is acquired by a married woman by an instrument in writing, the presumption is that the same is her separate property, and if acquired by such married woman and any other person the presumption is that she takes the part acquired by her, as tenant in common, unless a different intention is expressed in the instrument; except, that when any of such property is acquired by husband and wife by an instrument in which they are described as husband and wife, unless a different intention is expressed in the instrument, the presumption is that such property is the community property of said husband and wife. The presumptions in this section mentioned are conclusive in favor of any person dealing in good faith and for a valuable consideration with such married woman or her legal representatives or successors in interest, and regardless of any change in her marital status after acquisition of said property.

* * * (Enacted 1872. As amended Stats. 1889, c. 219, p. 328, Sec. 1; Stats. 1893, c. 62, p. 71, Sec. 1; Stats. 1897, c. 72, p. 63, Sec. 1; Stats. 1917, c. 581, p. 827, Sec. 1; Stats. 1923, c. 360, p. 746, Sec. 1; Stats. 1927, c. 487, p. 826, Sec. 1; Stats. 1935, c. 707, p. 1912, Sec. 1; Stats. 1941, c. 455, p. 1752, Sec. 1.)

Sec. 172. *Community personal property; management and control; restrictions on disposition.*

The husband has the management and control of the community personal property, with like absolute

power of disposition, other than testamentary, as he has of his separate estate; provided, however, that he cannot make a gift of such community personal property, or dispose of the same without a valuable consideration, or sell, convey, or encumber the furniture, furnishings, or fittings of the home, or the clothing or wearing apparel of the wife or minor children that is community, without the written consent of the wife. (Enacted 1872. As amended Stats. 1891, c. 220, p. 425, Sec. 1; Stats. 1901, c. 190, p. 598, Sec. 1; Stats. 1917, c. 583, p. 829, Sec. 1.)

Probate Code of California:

Sec. 201. *Title of surviving spouse; portion subject to testamentary disposition or succession.*

Upon the death of either husband or wife, one-half of the community property belongs to the surviving spouse; the other half is subject to the testamentary disposition of the decedent, and in the absence thereof goes to the surviving spouse subject to the provisions of sections 202 and 203 of this code. (Stats. 1931, c. 281, p. 595, Sec. 201, as amended Stats. 1935, c. 831, p. 2249, Sec. 2.)

Internal Revenue Code of 1939

Sec. 810. *Rate of Tax.*

A tax equal to the sum of the following percentages of the value of the net estate (determined as provided in section 812) shall be imposed upon the transfer of the net estate of every decedent, citizen or resident of

the United States, dying after the date of the enactment of this title. . . .

Sec. 811. *Gross Estate.*

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

(a) Decedent's Interest.—To the extent of the interest therein of the decedent at the time of his death;

* * *

(c) Transfers in Contemplation of, or Taking Effect at, Death.—

(1) General Rule.—To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise—

(A) in contemplation of his death; or

(B) under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death (i) the possession or enjoyment of, or the right to the income from, the property, or (ii) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom; or

(C) intended to take effect in possession or enjoyment at or after his death.

(2) Transfers Taking Effect at Death.—Transfers prior to October 8, 1949.—An interest in property of which the decedent made a transfer, on or about October 7, 1949, intended to take effect in possession or enjoyment at or after his death shall not be included in his gross estate under paragraph (1) (C) of this subsection unless the decedent has retained a reversionary interest in the property, arising by the express terms of the instrument of transfer and not by operation of law, and the value of such reversionary interest immediately before the death of the decedent exceeds 5 per centum of the value of such property. For the purpose of this paragraph, the term "reversionary interest" includes a possibility that property transferred by the decedent (A) may return to him or his estate, or (B) may be subject to a power of disposition by him, but such term does not include a possibility that the income alone from such property may return to him or become subject to a power of disposition by him. The value of a reversionary interest immediately before the death of the decedent shall be determined (without regard to the fact of the decedent's death) by usual methods of evaluation, including the use of tables of mortality and actuarial principles, pursuant to regulations prescribed by the Commissioner with the approval of the Secretary.

In determining the value of a possibility that property may be subject to a power of disposition by the decedent, such possibility shall be valued as if it were a possibility that such property may return to the decedent or his estate.

(3) Transfers Taking Effect at Death—Transfers After October 7, 1949.—An interest in property transferred by the decedent after October 7, 1949, shall be included in his gross estate under paragraph (1)(C) of this subsection (whether or not the decedent retained any right or interest in the property transferred) if and only if—

(A) possession or enjoyment of the property can, through ownership of such interest, be obtained only by surviving the decedent; or

(B) under alternative contingencies provided by the terms of the transfer, possession or enjoyment of the property can, through ownership of such interest, be obtained only by surviving the earlier to occur of (i) the decedent's death or (ii) some other event; and such other event did not in fact occur during the decedent's life.

Notwithstanding the foregoing sentence, an interest so transferred shall not be included in the decedent's gross estate under paragraph (1)(C) of this subsection if possession or enjoyment of the property could have been obtained by any beneficiary during the decedent's life through the exercise of a power of appointment (as defined in Section 811(f)(2)) which in fact was exercisable immediately prior to the decedent's death.

(d) Revocable Transfers.—

(1) Transfers after June 22, 1936.—To the extent of any interest therein of which the decedent has at

any time made a transfer (except in case of a bona fide sale for an adquate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, or where any such power is relinquished in contemplation of decedent's death;

(2) Transfers on or Prior to June 22, 1936.—To the extent of any interest therein of which the decedent has at any time made a transfer, by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend or revoke, or where the decedent relinquished any such power in contemplation of his death, except in case of a bone fide sale for an adequate and full consideration in money or money's worth. Except in the case of transfers made after June 22, 1936, no interest of the decedent of which he has made a transfer shall be included in the gross estate under paragraph (1) unless it is includible under this paragraph;

(3) Date of Existence of Power.—For the purposes of this subsection the power to alter, amend, or revoke shall be considered to exist on the date of the decedent's death even though the exercise of the power is subject to a precedent giving of notice or even

though the alteration, amendment, or revocation takes effect only on the expiration of a stated period after the exercise of the power, whether or not on or before the date of the decedent's death notice has been given or the power has been exercised. In such cases proper adjustment shall be made representing the interests which would have been excluded from the power if the decedent had lived, and for such purpose if the notice has not been given or the power has not been exercised on or before the date of his death, such notice shall be considered to have been given, or the power exercised, on the date of his death.

* * *

(g) Proceeds of Life Insurance.—

(1) Receivable by the Executor.—To the extent of the amount receivable by the executor as insurance under policies upon the life of the decedent.

(2) Receivable by Other Beneficiaries.—To the extent of the amount receivable by all other beneficiaries as insurance under policies upon the life of the decedent (A) purchased with premiums, or other consideration, paid directly or indirectly by the decedent, in proportion that the amount so paid by the decedent bears to the total premiums paid for the insurance, or (B) with respect to which the decedent possessed at his death any of the incidents of ownership, exercisable either alone or in conjunction with any other person. For the purposes of clause (A) of this paragraph, if the decedent transferred, by assignment or otherwise, a policy of insurance, the

amount paid directly or indirectly by the decedent shall be reduced by an amount which bears the same ratio to the amount paid directly or indirectly by the decedent as the consideration in money or money's worth received by the decedent for the transfer bears to the value of the policy at the time of the transfer. For the purposes of clause (B) of this paragraph, the term "incident of ownership" does not include a reversionary interest.

(3) Transfer Not a Gift.—The amount receivable under a policy of insurance transferred, by assignment or otherwise, by the decedent shall not be includible under paragraph (2)(A) if the transfer did not constitute a gift, in whole or in part, under Chapter 4, or, in case the transfer was made at a time when Chapter 4 was not in effect, would not have constituted a gift, in whole or in part, under such chapter had it been in effect at such time.

* * *

(26 U.S.C., 1952 ed., Secs. 810, 811)